In 1922, this corporation became involved, was adjudged a bankrupt, and in due course discharged (R. 31).

Petitioner, about the same time, was likewise adjudged a bankrupt personally, and discharged (R. 31).

In 1924, petitioner entered on his own account in the same line of business that his corporation had formerly transacted, i. e., handling grain on commission. He dealt with the old customers of the corporation, many of whom were his personal friends, and who had become customers of the corporation because of petitioner's connection with it (R. 31-34).

The Board of Tax Appeals found:

> "In order to re-establish his standing and credit, and to revive new business contacts with former customers of the E. L. Welch Company, the petitioner determined, as far as he was able, to reimburse certain creditors of the E. L. Welch Company" (R. 22).

Beginning in 1924, and continuing until 1928, he made substantial payments to the creditors of the corporation out of the earnings of his business (R. 31-33).

The Commissioner, on audit of his income tax returns, disallowed these payments to the creditors of the corporation as deductions, and assessed deficiencies for each of said years in the aggregate amount of Three Thousand Seventy-two and 96/100 Dollars ($3,072.96) on account thereof (R. 6-7, 10-14, 16-20). The Board of Tax Appeals sustained the Commissioner in the assessment of these deficiencies and the disallowance of these deductions (R. 21-25), and the Circuit Court of Appeals sustained the Board of Tax Appeals, dismissing the petition for review (R. 39-41).

It should be noted, however, that there was a complete lack of agreement as to the reason for the denial of these deductions.

The Commissioner ruled that they were "capital expenditures", and not expenses at all (R. 11).

This theory was, however, apparently (although not expressly) rejected by the Board of Tax Appeals. The reason of the Board of Tax Appeals is as follows:

> "If the payments relate at all to 'carrying on a trade or business' they still may not be allocated as expense of any particular year. Doubtless petitioner more quickly reestablished his standing and credit and built up his new business by reimbursing those who had lost money through a corporation dominated by him and his father, but we do not understand payments of such a nature to be ordinary and necessary business expenses" (R. 23).

The theory that these expenditures were not allocable to any particular year was rejected by the Circuit Court of Appeals, which said:

> "There may be room for argument and difference as to whether payments of this character, under the circumstances here, are 'necessary', or not. It would be rather clear that they would be helpful in a business way and that helpfulness might approach or reach necessity. However, we can see no possible basis upon which payments of this character can be treated as 'ordinary' expenses of his business * * *. In fact, they are very extraordinary * * * and not expenses of the business at all" (R. 40).

IV.

SPECIFICATION OF ERRORS.

The Circuit Court of Appeals erred in dismissing the petition for review and in sustaining the Board of Tax Appeals in

(1) Holding that there was a deficiency for each of the years 1924 to 1928, inclusive.

(2 Refusing to hold that the amounts paid by petitioner to the creditors of E. L. Welch Co[illegible]y were ordinary and necessary expenses in carrying on petitioner's business, and refusing to hold that such payments were proper deductions from income of said years.

V.

ARGUMENT.

The statutory provisions involved are Section 214 (a) (1) of the Revenue Acts of 1924 and 1926, and Section 23 (a) of the Revenue Act of 1928. These provisions of the statute are reproduced in full in the Appendix, page 18. These sections are all identical and provide that the taxpayer may have as a deduction from gross income "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." As stated by both Courts below, the only question is whether these payments to the creditors of the corporation were necessary and ordinary expenses of petitioner's business.

While there is no express finding in either Court, it is entirely clear from the reading of the record (R. 33-34) that if these payments had not been made, there would have been substantially no income from which to have deducted them. In other words, these payments resulted in a substantial income for each of the taxable years, and a resulting tax to the Government.

A

THERE IS A DIRECT CONFLICT OF DECISION BETWEEN THE EIGHTH AND THE FIFTH CIRCUITS.

The Court below, the Circuit Court of Appeals for the Eighth Circuit, reached a conclusion diametrically opposed to that of the Circuit Court of Appeals for the Fifth Circuit in *Harris vs. Lucas*, 48 Fed. (2nd), 187. The Court below did not, however, concede that its conclusion was opposed to that in the Harris case. In fact, it said:

> "They (the payments) are unlike the payments in Harris vs. Lucas * * *".

An analysis of the two cases shows, however, that there is no possibility of reconciling them. If there is a distinction, there is no difference. In the case below, after the bankruptcy of the corporation and consequent cancellation of its debts, the petitioner personally went into business. In the Harris case, after the bankruptcy of the corporation and consequent cancellation of its debts (composition agreement), the corporation itself went into business. In each case, the party desiring to increase its business paid debts which then had no legal existence on account of the bankruptcy. Yet, the Eighth Circuit holds such payments not to be proper deductions, while the Fifth Circuit holds that they are.

Will the Court compare the two cases:

8th Circuit.

Welch vs. Commissioner, (R. 39-40).

"The question is whether these expenses are 'ordinary and necessary', within the meaning of the statute. Words used in a statute are to be taken in their usual, everyday meaning, and this is particularly true of revenue statutes (United States vs. Kirby Lumber Co., 284 U. S. 1, 3; Woolford Realty Co. vs. Rose, 286 U. S. 319). The deductible expenses must be both 'necessary' and 'ordinary' (Lloyd vs. Commissioner, 55 Fed. (2d) 842, 844, C. C. A. 7). There may be room for argument and difference as to whether payments of this character, under the circumstances here, are 'necessary', or not. It would be rather clear that they would be helpful in a business way and that helpfulness might approach or reach necessity. However, we can see no possible basis upon which payments of this character can be treated as 'ordinary' expenses of his business (Robinson vs. Commissioner, 53 Fed. (2d) 810, 811, C. C. A. 8, and see Lloyd vs. Commissioner, 55 Fed. (2d) 842, C. C. A. 7, and Hubinger vs. Commisioner, 36 Fed. (2d) 724, 726, C. C. A. 2). In fact, they are very extraordinary payments, and not expenses of the business at all. They are unlike the payments in Harris vs. Lucas, 48 Fed. (2d) 187, C. C. A. 5, but are voluntary payments similar to those treated in Robinson vs. Commissioner, 53 Fed. (2d) 810, 811, C. C. A. 8, and Mastin vs. Commissioner, 28 Fed. (2d) 748, 753, C. C. A. 8. While these payments are highly commendable from an ethical standpoint, we are bound by the law as written."

5th Circuit.

Harris vs. Lucas, 48 Fed. (2nd), 187.

"It is evident that the words 'ordinary' and 'necessary' in the statute are not used conjunctively, and are not to be construed as requiring that an expense of a business to be deductible must be both ordinary and necessary in a narrow, technical sense. On the contrary, it is clear that Congress intended the statute to be broadly construed to facilitate business generally, so that any necessary expense, not actually a capital investment, incurred in good faith in a particular business, is to be considered an ordinary expense of that business. This in effect is the construction given the statute by the Treasury Department and the Courts.

* * * * *

"Of course, each case depends for decision upon its own facts, and it would be impossible to formulate a uniform rule to govern all cases. Generally speaking, business men should be free to exercise their ingenuity in devising methods of increasing business. This redounds to the benefit of the government by creating more taxable income. Considering the above-stated examples, it would seem clear by analogy that petitioner was entitled to deduct the amounts paid to its former creditors. It was under no legal obligation to make the payments, and they were made entirely to promote the business by restoring its credit with the wholesalers from whom it purchased goods.

* * * * * *

"It is perfectly plain that the payments did not constitute capital investment. On the contrary, the business was deprived of cash assets, and nothing was added to its saleable value. The payments may be classed as advertising expenditures as they secured credit not only from those to whom made but from the trade in general. They might be classed as bonuses paid to secure credit * * *".

It is apparent that the two cases cannot be reconciled, and that the Court below "has rendered a decision in conflict with the decision of another Circuit Court of Appeals on the same matter" (paragraph b, Section 3, Rule 38, Rules of this Court).

Bearing in mind that decisions of the Board of Tax Appeals are subject to review by ten different Courts of Appeals, it is apparent how necessary uniformity of decision in internal revenue cases becomes. At the present time, if the taxpayer lives in the Eighth Circuit, the Board of Tax Appeals must decide one way; if, in the Fifth Circuit, another way, and if, in any other Circuit, it must guess until such time as that Circuit of Appeals has spoken. This Court should definitely determine the law applying to such situation.

B.

THE DECISION OF THE CIRCUIT COURT OF APPEALS BELOW WAS INCORRECT.

It will not, we think, be disputed as a general proposition that business men should have a free hand to adopt such means as will result in increased business and increased income, resulting in increased revenue to the Government, and that the Government should not exercise a supervisory power over the methods adopted, or determine after the event whether the course adopted was wise or unwise, advisable or inadvisable, prudent or imprudent, so long as no law is violated. It is the taxpayer, whose investment is at stake, who should determine ways and means and not the Government.

The theory of the Board of Tax Appeals that these expenditures were not deductible, because not capable of allocation to any particular year, is obviously unsound under *Lucas vs. Ox Fibre Brush Company*, 281 U. S. 115. The Circuit Court of

Appeals did not adopt the view of the Board of Tax Appeals in that respect.

Under the terms of the Revenue Act, in order that an expense be properly deductible from gross income, it must be

(1) an expense attributable to "business",

(2) a "necessary" expense,

and*

(3) an "ordinary" expense.

(1)

WAS THIS A BUSINESS EXPENSE?

It is difficult to add anything to what the Harris case says in demonstrating that it was a business expense. The effort here by petitioner was to build up his business. By certain judicious payments, he accomplished this. Reading between the lines, it is apparent that if these payments had not been made, petitioner would not have had any income or business to tax. The Board of Tax Appeals in this case said:

> "Doubtless petitioner more quickly re-established his standing and credit and built up his new business by reimbursing those who had lost money * * *" (R. 23).

The Circuit Court of Appeals below said:

> "It would be rather clear that they (the payments) would be helpful in a business way and that helpfulness might approach or reach necessity" (R. 40).

It is impossible to distinguish the Harris case. There, a corporation paid certain of its old debts, which it was not required

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*Harris vs. Lucas, supra, holds that the words "ordinary" and "necessary" are not used conjunctively, but, on the contrary, are used disjunctively, although Lloyd vs. Commissioner, 55 Fed. (2nd), 842, holds that deductible expenses must be both "ordinary" and "necessary". This holding, however, was purely dictum, as the case was decided on the proposition that the expense involved was not a business expense.

to pay, to build up its business; here, petitioner paid certain debts of a corporation, dominated by him, and closely associated with his name in the public mind, which debts he was not legally required to pay, to build up his business. Of what consequence was it whose debts they originally were? This distinction loses all cogency because payment could not be enforced in either case, but the payment in each case was in a sense voluntary, and made as a matter of good business. Both the Board of Tax Appeals and the Circuit Court of Appeals clearly demonstrate by their reasoning that these were business expenditures, although each Court eventually rejects that conclusion.

How much more clearly were these business expenses than those involved in *Kornhauser vs. United States*, 276 U. S. 145, where this Court held that attorney's fees incurred in an accounting suit brought by a former law partner were business expenses, saying:

> "An expenditure for the purpose of obtaining or retaining taxable income does not seem like a personal expenditure" (p. 149).

The payments here are certainly more clearly business expenditures than those involved in *Commissioner vs. People's-Pittsburgh Trust Co.*, 60 Fed. (2nd), 187 (Third Circuit), where it was held that attorney's fees expended in defending a criminal charge of making false income tax returns were business expenditures rather than personal expenditures.

The Court of Appeals for the Sixth Circuit, in *American Rolling Mills Co. vs. Commissioner*, 41 Fed. (2nd), 314, held that contributions in the sum of Three Hundred Sixty Thousand Dollars ($360,000.00) to various civic organizations (Boy Scouts, American Legion, Y. M. C. A., etc.) were business expenditures. Certainly, these expenditures were voluntary in the sense that they could not have been compelled. They were made as a matter of good business. The Court said:

"The contention overlooks the fact that the contribution was not a philanthropy, but was a business expenditure to be reflected in increased earnings."

In *Corning Glass Works vs. Lucas*, 37 Fed. (2nd), 798, certiorari denied, 281 U. S. 742 (Court of Appeals, District of Columbia), it was held that a contribution of Twenty-five Thousand Dollars ($25,000.00) to the building fund of a hospital was a business expense, properly deductible.

The Board of Tax Appeals has consistently held that any expenditure reasonably tending to promote the business, earnings or good will of an enterprise is deductible as a business expense.*

Mastin vs. Commissioner, 28 Fed. (2nd), 748 (Eighth Circuit), relied on by the Court below, is not in point. It merely holds that expenditures for advertising real estate owned by a corporation, of which the taxpayer was a stockholder, were not business expenses of the taxpayer, but his personal expenses. The reason is clear. The taxpayer was not making the payment to better his own business, but to better the corporation's business. Obviously, therefore, it was not a business expense of the taxpayer.

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*Tickets to entertainments purchased from customers to promote good will, **McQuade's Appeal**, 4 B. T. A. 837; the cost of operating a yacht for the purpose of inducing customers to visit the plant, **Dickinson vs. Commissioner**, 8 B. T. A. 722; amounts paid by a brokerage firm to secure evidence to suppress bucket shops, **Pierce vs. Commissioner**, 18 B. T. A. 447; contribution to repair and enlarge a church attended by employees, **Peinsett Mills' Appeal**, 1 B. T. A. 6; contribution for erection of a school attended by employees' children, **Holt-Granite Mills Company's Appeal**, 1 B. T. A. 1246; fund for pensioning employees, **Hibbard, Spencer, Bartlett & Co. vs. Commissioner**, 5 B. T. A. 464; contribution to Chamber of Commerce, **Hirsch-Weis Manufacturing Co. vs. Commissioner**, 14 B. T. A. 796; payment of a note by a Jockey Club, which it was not legally obligated to pay to avoid revocation of license, **Louisiana Jockey Club, Inc., vs. Commissioner**, 13 B. T. A. 752; contribution of $1000.00 to the rebuilding of a church attended by taxpayer's employees, **Superior Pocahontas Coal Co. vs. Commissioner**, 7 B. T. A. 330. A contribution to the endowment fund of a college which had for its purpose the continuation of the college, as an institution * * * financially able to purchase petitioners product, **Yamhill Electric Co. vs. Commissioner**, 20 B. T. A. 1232.

Lloyd vs. Commissioner, 55 Fed. (2nd), 842 (Seventh Circuit), merely holds that attorney's fees expended by a taxpayer in prosecuting a slander suit against one who has slandered him personally were personal and not business expenditures. This case is not in point.

(2)

WERE THE EXPENDITURES "NECESSARY"?

The Circuit Court of Appeals below expressed doubt on this point. It seems to have entertained the view that in order that an expenditure be "necessary", it must be *absolutely* necessary, i. e., no option but to make it. The cases already cited under the last heading demonstrate that this is not the correct definition of the word, but beyond all this, this Court, more than a century ago, in *McCulloch vs. Maryland*, 4 Wheaton, 315, defined the word "necessary", as used in Section 8 of Article 1 of the Constitution, as follows:

> 'Is it true, that this is the sense in which the word 'necessary' is always used? Does it always import an absolute physical necessity, so strong, that one thing to which another may be termed necessary, cannot exist without the other? We think it does not. If reference be had to its use, in the common affairs of the world, or in approved authors, we find that it frequently imports no more than that one thing is convenient, or useful, or essential to another. To employ the means necessary to an end, is generally understood as employing any means calculated to produce the end, and not as being confined to those single means, without which the end would be entirely unattainable."

The word "necessary" in the Revenue Act means no more than that the expenditure shall be reasonably helpful in a busi-

ness way. So construed, it is clear these expenditures were necessary.

Robinson vs. Commissioner, 53 Fed. (2nd), 810 (Eighth Circuit), relied on by the Court below, is in no sense a parallel case. All that was there held was that the taxpayer could not get credit for taxes paid on somebody else's property, and which the taxpayer was not legally obligated to pay. However, if this case means that a taxpayer cannot take credit for a business expense unless he is legally obligated and compelled to make it, it is contrary to the holdings of every other Circuit.

(3)

WERE THE EXPENDITURES "ORDINARY"?

The Circuit Court of Appeals below says:

> "* * * we can see no possible basis upon which payments of this character can be treated as 'ordinary' expenses of his business * * *. In fact, they were very extraordinary payments * * *".

The Court was apparently of the view that the word "ordinary", as used in the statute, was synonymous with the words "usual" or "happening frequently" or "commonplace". That this is not the correct meaning of the word is made clear by *Kornhauser vs. United States,* 276 U. S. 145, where this Court said:

> "And it was an 'ordinary and necessary' expense, since a suit ordinarily and, as a general thing at least, necessarily requires the employment of counsel and payment of his charges."

It is clear, therefore, that it is not a question of whether an expense is a usual one, or commonly, or frequently incurred, but whether, *in the particular circumstances shown to have*

existed, it would be natural, or usual, or ordinary to have made the expenditure.

Referring again to *Commissioner vs. Peoples-Pittsburgh Trust Co.,* 60 Fed. (2nd), 187, it would, we think, be relatively uncommon and unusual for a man to hire a lawyer to defend him against the charge of making fraudulent tax returns. By this, we mean that it happens quite infrequently. Where, however, he is indicted for so doing, it is very usual and very common for him to employ a lawyer. In fact, it would be a most unusual case where he did not. Such attorney's fees were held "ordinary" expenses.

Granting that generally speaking it is unusual and even "extraordinary" for an individual to pay the debts of a corporation which have been discharged by bankruptcy, yet, if that individual were trying to continue in business and found that he could do no business and could get no credit (because the corporation was so closely linked with his name) unless the debts of the corporation were paid, it would, we think, be quite common, quite usual and quite "ordinary" for him to pay them.

In the sense attributed to the word by the Court below, none of the expenditures in any of the cases heretofore cited were "ordinary". In the broader sense, however, they were all "ordinary", and were so held. It is quite apparent that the Circuit Court of Appeals for the Eighth Circuit, contrary to the conclusions reached in other Circuits, has taken an unduly restricted view of what may be ordinary and necessary expenses.

The writ prayed for should be granted.

Respectfully submitted,

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APPENDIX.

Revenue Act of 1924, c. 234, 43 Stat. 253:

SEC. 214. (a) In computing net income there shall be allowed as deductions:

(1) All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity; * * *.

SEC. 215. (a) In computing net income no deduction shall in any case be allowed in respect of—

* * * * *

(2) Any amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate;

(3) Any amount expended in restoring property or in making good the exhaustion thereof for which an allowance is or has been made; * * *

Section 214 (a) (1) and Section 215 (a) (2) and (3) of the Revenue Act of 1926 (c. 27, 44 Stat. 9), and Section 23 (a) and Section 24 (a) (2) and (3) of the Revenue Act of 1928 (c. 852, 45 Stat. 791) are identical.